



TAX EXEMPT AND
GOVERNMENT ENTITIES
DIVISION

DEPARTMENT OF THE TREASURY
INTERNAL REVENUE SERVICE
WASHINGTON, D.C. 20224

Release Number: **201351024**
Release Date: 12/20/2013
Date: September 24, 2013
UIL Code: 501.04-00

Contact Person:

Identification Number:

Contact Number:

Employer Identification Number:

Form Required To Be Filed:

Tax Years:

Dear :

This is our final determination that you do not qualify for exemption from Federal income tax as an organization described in Internal Revenue Code section 501(c)(4). Recently, we sent you a letter in response to your application that proposed an adverse determination. The letter explained the facts, law and rationale, and gave you 30 days to file a protest. Since we did not receive a protest within the requisite 30 days, the proposed adverse determination is now final.

You must file Federal income tax returns on the form and for the years listed above within 30 days of this letter, unless you request an extension of time to file. File the returns in accordance with their instructions, and do not send them to this office. Failure to file the returns timely may result in a penalty.

We will make this letter and our proposed adverse determination letter available for public inspection under Code section 6110, after deleting certain identifying information. Please read the enclosed Notice 437, *Notice of Intention to Disclose*, and review the two attached letters that show our proposed deletions. If you disagree with our proposed deletions, follow the instructions in Notice 437. If you agree with our deletions, you do not need to take any further action.

If you have any questions about this letter, please contact the person whose name and telephone number are shown in the heading of this letter. If you have any questions about your Federal income tax status and responsibilities, please contact IRS Customer Service at

1-800-829-1040 or the IRS Customer Service number for businesses, 1-800-829-4933. The IRS Customer Service number for people with hearing impairments is 1-800-829-4059.

Sincerely,

Karen Schiller
Acting Director, Exempt Organizations
Rulings and Agreements

Enclosure
Notice 437
Redacted Proposed Adverse Determination Letter
Redacted Final Adverse Determination Letter



TAX EXEMPT AND
GOVERNMENT ENTITIES
DIVISION

DEPARTMENT OF THE TREASURY
INTERNAL REVENUE SERVICE
WASHINGTON, D.C. 20224

Date: August 12, 2013

UIL 501.04-00

Contact Person:

Identification Number:

Contact Number (until 8/24/13):

Contact Number (effective 8/24/13):

Fax Number (effective 8/24/13):

Employer Identification Number:

Legend:

C =
M =
X =

Dear :

We have considered your application for recognition of exemption from Federal income tax under Internal Revenue Code § 501(a). Based on the information provided, we have concluded that you do not qualify for exemption under Code § 501(c)(4). The basis for our conclusion is set forth below.

Facts

You are organized as a nonprofit corporation under State law. Your Articles of Incorporation state that your purposes include:

- (a) To secure dental services to individuals and groups and their families through the design of dental service coverage products and active involvement in the provision of such products through independent professional service providers.
- (b) To encourage, foster, and finance professional and scientific study and research in the general field of oral health; to make studies and conduct investigations designed to develop information pertaining to all aspects of dental service coverage plans; and to assist in the education of the public concerning the need for and advantages of oral health.

You were conceived of and formed by C, an organization that is recognized as exempt from federal income tax under § 501(c)(4). C is a member of the M and is a healthcare service

contractor providing dental benefits under contracts with participating dentists. C's primary business is facilitating the financing and delivery of oral healthcare programs.

You define your primary mission and public benefit to be that of improving oral health of the members of the public, and that your primary method of delivering such benefit will be through the dental benefits products you design and deliver to your clients.

You will focus on creating new benefits coverage models within the domain of oral health. Within this domain, you will pursue the following activities:

- Oral health science and analytics: You will acquire and build a core capability for epidemiological research related to oral health. Objectives include furthering understanding of the demographics of dental disease, the disease progression within individuals and outcomes related to preventative and restorative dental treatments.
- Dental benefits product development: Findings related to the above will be incorporated into the development of new, evidence-based dental benefits products. You will pursue innovative benefit structures within existing product lines, as well as development of new products to address underserved populations, including Medicaid, gap coverage, uninsured and individually-insured (vs. employer-insured) populations, and consumer products for distinct demographic groups (e.g., 25-55, pre-retirement, and post-retirement). Such products will be distributed by you in combination with or through other M plans.
- Specialized dental product administration: You will provide specialized product administration services in support of innovative benefits products, potentially including specialized underwriting, claims processes, network management, or marketing services. These services would be provided either to or in conjunction with other M plans that are using or distributing your products.
- Public awareness building: In addition to supporting the incorporation of dental science into dental benefits product design, you will develop and publish research papers in peer-reviewed journals and increase the level of interaction within the academic, industry and policy-making communities. You will also produce paid and earned media, targeting increased awareness and urgency among the public.

You will work with M members and their customers to tailor product designs to meet the specific needs of their patient and provider populations. You will contract with other M organizations (including C) to provide them innovative dental benefit coverage products and services through contracts with independent professional service providers. You will not provide any evidence based dental products other than through contracts with other M organizations. You will not provide any evidence based dental benefits products directly to the general public without contracts with independent professional service providers.

Your revenues are expected to be from the sale of evidence based benefit products and related benefits administration services to or through other M organizations. You told us that, since your innovative dental benefit coverage products and services have not yet been designed or

developed, the amounts to be received can only be estimated at this time, and the exact character of the services to be performed cannot be described with any specificity until such time as development activities have progressed toward a viable dental benefit coverage amount.

You have entered into a renewable five-year Service Mark License Agreement ("License Agreement") with M. The recitals under the License Agreement include a statement of your intent to--

... develop, offer, operate and provide dental benefits products and services, including, but not limited to, insurance benefits coverage product design, benefit plan administration, analytics, underwriting, claims processing, provider network design or management, and marketing exclusively to, through, on behalf of, or in conjunction with M or one or more of its Member Companies.

Under the License Agreement, M grants you a non-exclusive license to use its Service Marks, subject to certain conditions. One of these conditions, in § 1.1(h) of the license agreement, states:

All products and services developed, offered or provided by Licensee shall be offered, distributed or provided exclusively to, through, on behalf of or in conjunction with the M or one or more Member Companies of the M and, if permitted under written agreement with applicable Member Company, may be provided directly by [you] to the customers of such Member Company; provided, however, that all products and services offered, distributed, or provided as described in this Section 1.1(h) shall be offered, distributed or provided only as M branded products or services, and only in compliance with Section 1.1.

The License Agreement states that you will pay M a certain annual license fee equal to the greater of \$x or the amount of dues a M Member Company would pay M having the same operating results. The License Agreement also states that you may advertise your products and services jointly with other M member and non-member entities only with the prior written approval of the M.

C provided you with initial funding, and intends to provide further funding for your operations. C may also provide data to support your epidemiological research and may collaborate on studies or testing of new product ideas. You state that "[C]'s relationship with [you] will be the same as [your relationship with] any other [M] member – as a customer for the innovative oral health products developed by [you]." Currently, you have no agreements with C.

Your bylaws provide for seven or eight directors. Four directors must be "individuals who are knowledgeable and experienced in the field of oral health or the provision of dental benefits and who have no current employment relationship or other affiliation with C." (You refer to these directors as the "Independent Directors.") Three directors must be the Chief Executive Officer of C, the Chairman of the C Board of Directors, plus a third individual designated by the C Board

of Directors. (You refer to these directors as the "C Directors.") In addition, your Board may add your Chief Executive Officer as the eighth director.

Law

I.R.C. § 501(c)(4) provides for exemption from federal income taxation for civic leagues or organizations that are operated exclusively for the promotion of social welfare and not organized for profit.

Treas. Reg. § 1.501(c)(4)-1(a)(2)(i) provides that an organization is operated exclusively for the promotion of social welfare if it is primarily engaged in promoting in some way the common good and general welfare of the people of the community. An organization embraced within this section is one which is operated primarily for the purpose of bringing about civic betterments and social improvements.

Treas. Reg. § 1.501(c)(4)-1(a)(2)(ii) provides that an organization is not operated primarily for the promotion of social welfare if its primary activity is carrying on a business with the general public in a manner similar to organizations that are operated for profit.

Rev. Rul. 54-394, 1954-2 C.B. 131, concerns an organization that furnishes television reception for its members on a cooperative basis in an area not readily adaptable to ordinary reception. Members are required to contract for services and to pay installation fees. Under these facts, the Service ruled that the organization was not entitled to exemption under the predecessor statute to § 501(c)(4). When an organization's only activity is to provide television reception on a cooperative basis to its members, who contract and pay for such services, such organization is held to operate for the benefit of its members rather than for the promotion of the welfare of mankind.

Rev. Rul. 62-167, 1962-2 C.B. 142, concerns an organization, the purpose of which is to construct and maintain a reflector-type television station, capable of receiving signals of television stations and reproducing these signals so that satisfactory television would be available to the community in general. Membership is available to all persons in the area and the organization's income is derived from membership fees and donations. The reflector-type equipment received signals from three television stations and retransmitted these signals into the community. The signals retransmitted by the reflector-type apparatus were available to any television in the community. Under these circumstances, the Service ruled that the organization was entitled to exemption as an organization described in § 501(c)(4). Unlike the situation in Rev. Rul. 54-394 in which television services are available only to members of the organization and only pursuant to a contract requiring the payment of membership fees and monthly maintenance charges, here the organization operates its system for the benefit of all television owners in the community and memberships and contributions are obtained on a voluntary basis.

Rev. Rul. 79-316, 1979-2 C.B. 228, concerns an organization that was formed to prevent liquid spills within a city port area and to develop a program for the containment and cleanup of liquid spills that do occur. Its membership includes business firms, primarily oil and chemical companies which store or ship liquids in the port area. The organization is an approved

discharge cleanup organization under the applicable state law dealing with the prevention of oil spills. As such, it is required under state law to clean up spills of unknown source upon request of the appropriate state authorities, but is not required to clean up spills of identified nonmembers. The organization visits members' facilities to give technical assistance and to recommend improvements in handling liquids. In addition, the organization cleans up liquid spillage within the city port area. When a member is responsible for spillage, the organization charges the member a fee equal to the cost of labor, supplies, and equipment used in the cleanup. A nonmember identified as being responsible for a spill also must pay a fee to cover the cost of labor, supplies, and equipment used. There are no commercial cleanup companies operating in the entire geographical region where the port is located. Although there are a few commercial companies providing similar services in other geographical areas, the operation of a commercial cleanup organization is not economically feasible in the port area served by the organization. Under these facts, the Service ruled that the organization qualifies as a social welfare organization under § 501(c)(4). By preventing and cleaning up spills that endanger marine life and foul recreational beaches and shorefront property in the port area, the organization is primarily engaged in activities designed to benefit all inhabitants of the community served by it. The organization's cleanup services are equally available to members and nonmembers, and both members and nonmembers are charged for the cost of labor, supplies, and equipment used in the cleanup of their spills. By cleaning up spills of members and nonmembers, the organization is acting to prevent deterioration of the port community and not merely to prevent damage to facilities of its members. Thus, any effect the organization has in aiding compliance with applicable state law and in lowering insurance rates in the port area extends to all members of the port community, not just to members of the organization. Therefore, any benefits to members can properly be characterized as incidental to the primary activity of the organization.

Rev. Proc. 2013-9, 2013-2 I.R.B. 255, § 4.01, provides that the Internal Revenue Service will recognize the tax-exempt status of an organization only if its application and supporting documents establish that it meets the particular requirements of the section under which exemption from federal income tax is claimed. Section 4.03 provides that exempt status may be recognized in advance of the organization's operations if its proposed operations are described in sufficient detail to permit a conclusion that it will clearly meet the particular requirements for exemption pursuant to the section of the Code under which exemption is claimed. Section 4.03(2) states that the organization must fully describe all of the activities in which it expects to engage, including the standards, criteria, procedures or other means adopted or planned for carrying out the activities, the anticipated sources of receipts, and the nature of contemplated expenditures.

In *Comm'r v. Lake Forest Inc.*, 305 F.2d 814 (4th Cir. 1962), a nonprofit membership corporation purchased two housing projects from the federal government to use as homes for its members, consisting of inadequately housed war veterans. In reversing the Tax Court, the Court of Appeals concluded that the organization did not qualify for exemption under § 501(c)(4), saying that the housing project is not "civic" but simply a private cooperative enterprise. The court concluded that Lake Forest did not meet the dictionary definition of "civic" because, while the advantages offered by Lake Forest are available to all citizens eligible for membership, the benefits were not municipal or public in nature. The court also concluded that

the organization did not meet the dictionary definition of "social" or "welfare" because it did not propose to offer a service or program for the direct betterment or improvement of the community as a whole. While Lake Forest does furnish housing to a certain group of citizens, it does not do so on a community basis. It is a public-spirited but privately devoted endeavor. Its work in part incidentally redounds to society but this is not the "social welfare" of the tax statute.

Contracting Plumbers Coop. Restoration Corp. v United States, 488 F.2d 684 (2d Cir. 1973), concerns an organization formed by a group of plumbers to ensure the efficient repair of "cuts" in city streets, curbs, and sidewalks made in the process of providing plumbing services. The court concluded that the organization was not tax-exempt under § 501(c)(4), because it served the private interests of its members. The court characterized the plumbers' interest in the organization as a substantial business interest. The court found that each member of the cooperative enjoys these economic benefits precisely to the extent that he uses, and pays for, its restoration services. Because the benefits to its members were substantial and proportional to their financial involvement, the court concluded that the organization was not primarily devoted to the common good as required by § 501(c)(4).

Analysis

To be described in § 501(c)(4) you must be operated exclusively for the promotion of social welfare. Treas. Reg. § 1.501(c)(4)-1(a)(2)(i) explains that an organization will be considered to be operated exclusively for the promotion of social welfare only if it is primarily engaged in promoting in some way the common good and general welfare of the people of the community. Based on the information you provided us, we find that you are not primarily engaged in promoting the common good and general welfare of the people of the community. Rather, you are primarily engaged in serving the private business interests of M and its member companies.

You were organized by C, an M member company, for the purpose of developing dental benefit products for it and other M member companies. You entered into a License Agreement with M for the purpose of offering, distributing, and providing your dental benefit products, under M's service marks, exclusively to or through M and its member companies. In conjunction with the provision of dental benefit products, you contemplate providing specialized administrative services (such as underwriting, claims processing, network management, and marketing) for a fee exclusively to M member companies.

Your dental benefits products and administrative services are not available to all dental plans, but only to the plans of M member companies. Thus, like the organization described in Rev. Rul. 54-394 (which is not exempt under § 501(c)(4) because it provides services only to its members), and unlike the organization described in Rev. Rul. 62-167 (which is exempt under § 501(c)(4) because it provides services to the entire community), you do not promote the welfare of the people of the community and, thus, do not qualify for exemption under § 501(c)(4).

Like the activities of the organization described in *Contracting Plumbers Coop. Restoration Corp.* (which activities primarily served the private business interests of its paying members), your activities – the development of dental benefits products for M member companies and the provision of specialized administrative services with respect to those products – serve the

private business interests of those M member companies, which enjoy such benefits precisely to the extent that they pay for such products and services. Unlike the organization described in Rev. Rul. 79-316 (whose services were equally available to both members and nonmembers on similar terms), your products and services are not available to all dental plans. Rather, they will be offered, distributed, or provided exclusively to M or one of its member companies. Thus, because your activities primarily serve the private business interests of M and its member companies, you do not qualify for exemption under § 501(c)(4).

Although your activities are intended to further the understanding of the demographics of dental disease and to incorporate such findings into the development of new, evidence-based dental benefits products, such activities, like those of the respondent in *Comm'r v. Lake Forest, Inc.*, are essentially a privately-devoted endeavor for the benefit of M and its member companies. Although such research might incidentally redound to society, your dental benefits products development is not "social welfare" within the meaning of § 501(c)(4) because it is not intended for the direct benefit or improvement of the community as a whole, but only for the benefit of the subscribers to the M plans. And while you may engage in some "public awareness building" activities that might serve to promote the common good and general welfare of the people of the community, it does not appear that such activities constitute your primary activity.

An organization that carries on a business with the general public in a manner similar to organizations which are operated for profit is not operated primarily for the promotion of social welfare. See Treas. Reg. § 1.501(c)(4)-1(a)(2)(ii). The development of dental benefits products and the provision of administrative services like underwriting, claims processing, network management, and marketing to unrelated exempt or nonexempt organizations for a fee is generally considered a commercial trade or business. You have not supplied us with any information to show that you will conduct such activities other than in a manner similar to organizations operated for profit.

Section 4.03 of Rev. Proc. 2013-9 states that the Service will recognize the tax-exempt status of an organization only if its proposed activities are described in sufficient detail to permit a conclusion that the organization will clearly meet the requirements for exemption pursuant to the section of the Code under which exemption is claimed. You failed to describe your dental benefits products with any specificity. You failed to describe how you will market your dental benefits products. You also failed to describe your administrative services and the terms under which they will be provided. Furthermore, you could not accurately anticipate your sources of revenue. Instead, you told us that "since the ... innovative dental coverage products and services have not yet been designed or developed, the amounts to be received can only be estimated at this time, and the exact character of the services to be performed cannot be described with any specificity until such time as development activities have progressed toward a viable dental benefit coverage approach." Since you have not fully described your products, services, and anticipated sources of receipts, we cannot conclude that you will be operated in a manner other than that of an organization operated for profit. Consequently, we cannot recognize you as exempt under § 501(c)(4).

Conclusion

Because you are not primarily engaged in promoting the common good and general welfare of the people of the community under § 501(c)(4)-1(a)(2)(i) of the regulations, you do not qualify for recognition of exemption as an organization described in § 501(c)(4) of the Code.

You have the right to file a protest if you believe this determination is incorrect. To protest, you must submit a statement of your views and fully explain your reasoning. You must submit the statement, signed by one of your officers, within 30 days from the date of this letter. We will consider your statement and decide if the information affects our determination.

Your protest statement should be accompanied by the following declaration:

Under penalties of perjury, I declare that I have examined this protest statement, including accompanying documents, and, to the best of my knowledge and belief, the statement contains all the relevant facts, and such facts are true, correct, and complete.

You also have a right to request a conference to discuss your protest. This request should be made when you file your protest statement. An attorney, certified public accountant, or an individual enrolled to practice before the Internal Revenue Service may represent you. If you want representation during the conference procedures, you must file a proper power of attorney, Form 2848, *Power of Attorney and Declaration of Representative*, if you have not already done so. For more information about representation, see Publication 947, *Practice before the IRS and Power of Attorney*. All forms and publications mentioned in this letter can be found at www.irs.gov, Forms and Publications.

If you do not intend to protest this determination, you do not need to take any further action. If we do not hear from you within 30 days, we will issue a final adverse determination letter. That letter will provide information about filing tax returns and other matters.

Please send your protest statement, Form 2848 and any supporting documents to this address:

You may also fax your statement using the fax number shown in the heading of this letter. If you fax your statement, please call the person identified in the heading of this letter to confirm that he or she received your fax.

If you have any questions, please contact the person whose name and telephone number are shown in the heading of this letter.

Sincerely,

Karen Schiller
Acting Director,
Exempt Organizations
Rulings and Agreements